Switzerland

Jonas Sigrist and Pascale Schwizer
Pestalozzi Attorneys at Law Ltd, Zurich

Jonas Sigrist and Pascale Schwizer of Pestalozzi Attorneys at Law Ltd, Zurich, discuss the status of the implementation of Pillar Two in Switzerland to date, and the divergence of the GloBE income rule from the income subject to Swiss corporate income tax.

Background

BEPS Action 1 on the Taxation of the Digital Economy

In 2015, the Organisation for Economic Co-operation and Development (OECD) released its final report on Base Erosion and Profit Shifting (BEPS).[1] The BEPS project is a package of measures with 15 specific actions that tackle tax avoidance and aim to ensure the taxation of profits where economic activities and value creation take place.[2] Action 1, which addresses the tax challenges arising from digitalization and is commonly known as the Taxation of the Digital Economy, is based on a Two Pillar concept.[3] On October 14, 2020, the OECD/G-20 Inclusive Framework on BEPS published a report on the Pillar Two Blueprint. On October 8, 2021, the Inclusive Framework issued its Statement on a Two Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy, which was agreed by 137 member jurisdictions, including Switzerland, by November 4, 2021.[4]

The Two Pillar concept for the Taxation of the Digital Economy is generally referred to as "BEPS 2.0." In a nutshell, Pillar One provides for a shifting of taxing rights to market jurisdictions and affects entities with more than 20 billion euros ($21.4 billion) in consolidated annual revenue and a profit margin of more than 10%. Pillar Two provides for a global minimum 15% rate of taxation for multinationals with consolidated annual revenues of more than 750 million euros.

[1] *BEPS 2015 Final Reports, published on https://www.oecd.org/ctp/beps-2015-final-reports.htm, last visited May 27, 2022.*
[2] *For further reference, visit: https://www.oecd.org/tax/beps/beps-actions/, last visited May 25, 2022.*
[3] *Website of the OECD regarding Action 1, https://www.oecd.org/tax/beps/beps-actions/action1/, last visited May 23, 2022.*
[4] *Statement on a Two Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy, published on https://www.oecd.org/tax/beps/statement-on-a-two-pillar-solution-to-address-the-tax-challenges-arising-from-the-digitalisation-of-the-economy-october-2021.htm, last visited May 27, 2022.*

Impact of BEPS 2.0 on Switzerland

While Pillar One is expected to affect only a handful of large multinationals, Pillar Two is of particular interest for Switzerland, because some 200 multinationals headquartered in Switzerland and a multitude of Swiss subsidiaries of foreign multinationals will be affected by the global minimum taxation rules.[5]

Switzerland is well known for its competitive corporate tax rates. As of January 1, 2020, a corporate tax reform became effective in Switzerland that abolished the previously existing special tax regimes, including the regimes for holding and international trading companies. At the same time, this reform introduced tax reliefs that are widely accepted as being in compliance with the OECD modified nexus approach, including a patent box and a super deduction for research and development (R&D Super-Deduction).[6] The corporate tax reform was designed to improve Switzerland's compliance with international tax standards while at the same time maintaining and further expanding its tax competitiveness. The reform provided the Swiss cantons with additional financial latitude, allowing them to reduce their ordinary corporate tax rates.

Against this background, many cantons have significantly reduced their ordinary corporate income tax rates over the last few years. In 2021, the aggregate ordinary corporate income tax rates on profit before taxes ranged from around 11.8% to 22.8%.[7] The average aggregate rate of corporate income taxes (including federal income tax) on profit before taxes across the Swiss cantons is slightly below 15%.[8] A company with its registered office and place of effective management in Switzerland that is subject to a higher corporate income tax rate may, however, still be affected by Pillar Two because of:

- A potentially lower tax basis under Swiss statutory accounting and corporate tax rules as compared to the Global Anti-Base Erosion income relevant for Pillar Two (for more details see below);
- A lower tax basis resulting from preferential taxation, for example, in connection with the patent box, the R&D Super-Deduction, or the deductibility of amortization following a tax neutral basis step-up; and/or
- A lower tax rate resulting from the allocation of a portion of the company's profit to another Swiss canton with a lower tax rate under inter-cantonal tax allocation rules.

Switzerland is a relatively small country in terms of geographical size and population,[9] but has a considerable economy in terms of both size (its gross domestic product (GDP) of some $750 billion is larger than that of the smallest of the G-20 countries) and innovation (Switzerland leads the Global Innovation Index). While

---

[5] *Press release from the Federal Department of Finance dated July 1, 2021,* *https://www.efd.admin.ch/efd/en/home/the-fdf/nsb-news_list.msg-id-84315.html, last visited May 25, 2022.*

[6] *Press release from the Swiss Federal Council on the implementation of November 13, 2019,* *https://www.admin.ch/gov/en/start/documentation/media-releases/media-releases-federal-council.msg-id-77046.html, last visited May 27, 2022.*

[7] *Pascal Hinny, Steuerrecht 2022, Zurich 2022, Steuerbelastung in den Kantonen p. 2484-2485.*

[8] *Average corporate income tax rates in Switzerland between 2012-2022, Schweiz -* *https://de.statista.com/statistik/daten/studie/513550/umfrage/gewinnsteuersatz-in-der-schweiz, last visited May 20, 2022.*

[9] *Switzerland has a total surface of 41,285 square kilometers and had some 8.6 million inhabitants per the end of 2020 according to the Swiss Federal Statistical Office.*

there are widely shared concerns in Switzerland about the potential negative impact of the Pillar Two concept on tax competition and innovation, there is also broad agreement that Switzerland cannot isolate itself from international norms. Recently, there has also been some feeling of relief in view of the fact that BEPS 2.0 entails only a limited shift in taxing rights to market jurisdictions and a rather modest global minimum tax rate of 15%. Against this background, Switzerland joined the Inclusive Framework Statement while explicitly maintaining its reservations. "Switzerland is committed to rules that foster innovation and prosperity, that are applied uniformly worldwide and that are subject to a dispute settlement mechanism."[10]

Switzerland aims to provide multinationals with legal certainty and plans to implement the Pillar Two rules in its domestic legislation as soon as possible. In compliance with Switzerland's legislative process, however, the implementation of the Pillar Two rules cannot be expected before 2024 (for more details, see below). The implementation of Pillar Two in Swiss domestic law will prevent multinationals from being exposed to additional tax procedures abroad, which would also result in additional costs and tied resources. Besides that, if Switzerland were not to implement the Pillar Two rules in its domestic law, multinationals could be subject to a top-up tax abroad, which would ultimately result in tax revenues bypassing Switzerland and flowing to foreign jurisdictions.

Pillar Two – Global Minimum Tax

Overview

The details of the Pillar Two rules are outlined in the Global Anti-Base Erosion Model Rules, which were published by the OECD on December 20, 2021 (the Model Rules)[11] and in the commentary on the Model Rules, which were published by the OECD on March 11, 2022 (the Commentary on the Model Rules).[12] The 15% global minimum taxation is to be achieved based on:

- The Income Inclusion Rule (IIR), which imposes a top-up tax on a parent entity of a multinational group with respect to low taxed-income of a group subsidiary or permanent establishment (PE) (a Constituent Entity);[13]
- The Undertaxed Payments Rule (UTPR), which denies deductions or requires an adjustment to the extent low-taxed income of a Constituent Entity is not taxed under the IIR;

---

[10] *Press release from the Federal Department of Finance dated October 8, 2021, https://www.admin.ch/gov/de/start/dokumentation/medienmitteilungen.msg-id-85410.html, last viewed May 27, 2022.*

[11] *Tax Challenges Arising from the Digitalization of the Economy Global Anti-Base Erosion Model Rules (Pillar Two), Inclusive Framework on BEPS, OECD/G20 Base erosion and Profit Shifting Project (Model Rules), approved by the OECD/G20 on December 14, 2021, https://www.oecd.org/tax/beps/tax-challenges-arising-from-the-digitalisation-of-the-economy-global-anti-base-erosion-model-rules-pillar-two.pdf, last visited May 25, 2022.*

[12] *Tax Challenges Arising from the Digitalization of the Economy – Commentary to the Global Anti-Base Erosion Model Rules (Pillar Two), Inclusive Framework on BEPS,, approved by the OECD/G20 on March 11, 2022, https://www.oecd.org/tax/beps/tax-challenges-arising-from-the-digitalisation-of-the-economy-global-anti-base-erosion-model-rules-pillar-two-commentary.pdf, last visited May 25, 2022.*

[13] *As defined in art. 1.3 of the Model Rules.*

- The Subject to Tax Rule (STTR), which is an overriding treaty-based rule that allows source jurisdictions to impose limited source taxation on certain payments from affiliates subject to low (or no) taxation; and
- The Switch-Over Rule (SoR), which is a treaty-based rule that permits a residence jurisdiction to switch from an exemption to a credit method of relieving double taxation.

Essentially, Pillar Two aims to ensure that all participating jurisdictions impose a global minimum tax of 15% on Constituent Entities of multinational groups. If a jurisdiction does not tax a relevant Constituent Entity at a rate of at least 15% (for example, by way of an ordinary income tax or a domestic top-up tax), the IIR or the UTPR will allow other jurisdictions to levy taxes to ensure a minimum global 15% taxation. The IIR provides for a "Top-Down" approach to determine the jurisdiction that has the right to levy such taxes.[14] This means that, if the jurisdiction of tax residence of a Constituent Entity does not ensure the minimum taxation, the jurisdiction of the Ultimate Parent Entity (or of the next Intermediate Parent Entity) generally has the right to levy the additional taxes.[15] The UTPR, which allows any jurisdiction in which one or more Constituent Entities are tax resident to levy additional taxes or deny deductions on a pro rata basis, applies only if the IIR does not apply.[16]

The IIR and the UTPR are commonly referred to as the GloBE Rules. The GloBE Rules have to be implemented in Switzerland's domestic law based on the Model Rules, whereas the STTR and the SoR may be introduced through Switzerland's many tax treaties with other jurisdictions.

Scope of Minimum Taxation

Multinational enterprise groups fall within the scope of the Pillar Two rules if they have consolidated annual revenues of at least 750 million euros in at least two of the four preceding fiscal years (MNE Groups).[17] Unlike Pillar One, Pillar Two generally does not provide for industry specific exemptions, except with respect to income deriving from international shipping. (Entities generating income from the transportation of passengers or cargo by ships via inland waterways within the same jurisdiction are, however, not excluded from the Pillar Two measures.[18]) Nor does Pillar Two apply to governmental entities, international organizations, non-profit organizations, pension funds and investment funds or real estate investment vehicles that are Ultimate Parent Entities (Excluded Entities).[19] However, the revenue of Excluded Entities is still taken into consideration in calculating the revenue threshold of an MNE Group.[20] Furthermore, a de

---

[14] Model Rules, p. 9 and pp. 24 et seq.; Overview of the Key Operating Provisions of the Globe Rules ("Fact Sheet Model Rules"), https://www.oecd.org/tax/beps/pillar-two-GloBE-rules-fact-sheets.pdf, last visited May 25, 2022, p. 6/6.

[15] Regarding the detailed rules, reference is made to art. 2.1 -2.3. Model Rules.

[16] Model Rules, art. 2.4.

[17] Model Rules, art. 1.1.1.

[18] Model Rules, art. 3.3.2.

[19] Model Rules, art. 1.5.

[20] Fact Sheet Model Rules, p. 2/6.

minimis exemption applies to jurisdictions in which an MNE Group has less than 10 million euros of (average GloBE) revenue and less than 1 million euros of (average GloBE) income.[21]

Basis for the Calculation of the Top-up Tax

To determine if the income of a Constituent Entity within a jurisdiction is subject to a minimum rate of 15%, the Global Anti-Base Erosion income (GloBE Income) as well as the current tax expense accrued in the annual financials (Covered Taxes) must be determined for each jurisdiction in which an MNE Group has a Constituent Entity. If the percentage arrived at by dividing the Covered Taxes by the GloBE Income is less than 15% in a relevant jurisdiction, that jurisdiction may levy a top-up tax. If the jurisdiction does not impose such a top-up tax, other jurisdictions may levy taxes under the IIR or the UTPR.

GloBE Income and its Divergence from the Income Subject to Swiss Corporate Income Tax

The relevant GloBE Income is to be determined based on an Acceptable Financial Accounting Standard,[22] in particular IFRS or U.S. GAAP. The Swiss Accounting and Reporting Recommendations (Swiss GAAP FER)[23] should also be considered an Acceptable Financial Accounting Standard.[24] Swiss GAAP FER, which is based on a true and fair view approach, is not to be confused with the Swiss statutory accounting rules under the Swiss Code of Obligations.[25]

The Swiss statutory accounting rules focus on creditor rather than on investor protection and do not adhere to the true and fair view principle. Specifically, subject to certain limitations, the Swiss statutory accounting rules allow assets to be understated and liabilities to be overstated, and to provide for excessive depreciation and amortization, resulting in hidden reserves. It is, therefore, possible that financial reporting in accordance with the Swiss statutory accounting rules will often result in a Material Competitive Distortion,[26] requiring an adjustment to achieve alignment with the corresponding Acceptable Financial Accounting Standard principle or procedure for purposes of determining GloBE Income.

Subject to a few specific adjustment rules, a Swiss company's standalone financial statements drawn-up in accordance with Swiss statutory accounting rules (rather than an Acceptable Financial Accounting Standard) are relevant to the determination of the profit subject to corporate income taxation in Switzerland.[27] Determining the GloBE income or loss of a Swiss resident Constituent Entity therefore requires specific knowledge of the Acceptable Financial Accounting Standards and where they conflict with Swiss statutory accounting rules. This may represent a significant challenge for Swiss Constituent Entities and an even greater challenge for the cantonal tax authorities who will be responsible for assessing or reviewing

---

[21] *Model Rules, art. 5.5.1*

[22] *As defined in art. 10.1 nos. 3 et seq. on p. 193 of the Model Rules.*

[23] *Available on https://www.fer.ch/en/, last viewed May 27, 2022.*

[24] *Cf. Daniel Gentsch/Alain Horat, Principles of Calculation of the Globe Tax Rate, ExpertFocus April 2022, p. 132.*

[25] *Swiss Federal Act on the Amendment of the Swiss Civil Code (Part Five: The Code of Obligations) of March 30, 1911, arts. 957 et seq.*

[26] *As defined in art. 10.1 nos. 58 et seq. on p. 203 of the Model Rules.*

[27] *Swiss Federal Direct Tax Act of Dec. 14, 1990 ("DBG"), arts. 58 et seq.; Federal Act on the Harmonization of the Direct Taxes of the Cantons and Municipalities of Dec. 14, 1990 (StHG), arts. 24 et seq.*

GloBE International Returns but may well not have the requisite knowledge or resources. This is particularly true for the rural cantons in which there may be only a few taxpayers that are required to file GloBE International Returns.

The Model Rules also provide for a number of adjustments to the financial results computed in accordance with an Acceptable Financial Accounting Standard for purposes of determining the GloBE income.[28] However, these adjustments are often not consistent with Swiss domestic tax rules, resulting in a tax burden for GloBE purposes different from the tax burden under Swiss corporate tax law. For example:

- Swiss tax law provides for a relief with respect to income from qualifying shareholdings that, on the one hand, also applies to short-term and portfolio shareholdings with a fair market value of at least 1 million Swiss francs ($1.02 million) and, on the other, is limited to "net" income after the deduction of financing and administration costs.[29] On the contrary, under the Model Rules, Excluded Dividends do not include dividends from portfolio shareholdings with a holding period of less than one year but do include the entire gross dividend amount in the case of other dividends.[30]
- Recaptures and revaluation gains in the context of the alienation of qualifying shareholdings are taxable for Swiss federal corporate income tax purposes, while capital losses and depreciation with respect to qualifying shareholdings are classified as tax-deductible expenses.[31] This will result in a deviation from the GloBE income calculation rules where such items are classified as, respectively, Excluded Equity Gains or Losses under the Model Rules.[32]
- It is generally possible to make a tax-neutral transfer of a fixed business asset or an entire business unit between Swiss Constituent Entities in the same MNE Group by maintaining the asset's existing tax basis.[33] If such a tax neutral transfer results in a loss for the transferring Swiss Constituent Entity, that entity would be required to adjust its income for GloBE purposes under the arm's length principle.[34]

Covered Taxes

Covered Taxes for purposes of the calculation of the minimum taxation include all types of taxes levied on the income or profits of a Constituent Entity. It is expected that, in addition to the ordinary corporate income taxes, the following Swiss taxes will be regarded as giving rise to relevant tax expenses: capital taxes on net equity; church taxes; real estate capital gains taxes; and foreign withholding taxes that are final and for which a refund cannot be claimed. Swiss top-up taxes, stamp duties and other transaction taxes, value-added taxes,

---

[28] *Model Rules, art. 3.2.*

[29] *DBG, arts. 69 et seq., StHG, art. 28(1).*

[30] *Commentary to the Model Rules, art. 3.2.1(b).*

[31] *DBG, arts. 62(4) and 70(2)(c).*

[32] *Commentary to the Model Rules, art. 3.2.1(c)*

[33] *DBG, art. 61.*

[34] *Commentary to the Model Rules, art. 3.2.3., no. 107.*

customs duties, and social security contributions are, however, not considered Covered Taxes under Pillar Two and will therefore not be included in the minimum taxation calculation.[35]

GloBE Tax Return

Constituent Entities are generally required to file separate tax returns (GloBE Information Returns) in the jurisdictions that have implemented Pillar Two.[36] However, the obligation to file in all relevant jurisdictions does not apply if it is possible to file the GloBE Information Return in a jurisdiction that will provide the other jurisdictions with the relevant information based on an automatic exchange of information agreement ("Qualified Competent Authority Agreement").[37] Switzerland plans to implement Qualified Competent Authority Agreements with all other participating jurisdictions, so that Constituent Entities will not be required to file additional GloBE Information Returns in Switzerland.

The GloBE Information Return will have to be filed within 18 months after the last day of the reporting fiscal year in a standard template and will have to include the requisite information for all relevant jurisdictions to enable an assessment to be made as to whether the minimum taxation standard is met.[38] If the filing obligation is not complied with and the appropriate share of taxes is not paid, the penalties and sanctions of the relevant jurisdiction will apply.[39] While the sanctions for noncompliance have not yet been specified, sanctions will certainly be introduced in Switzerland in parallel with the implementation of Pillar Two.

Implementation of Pillar Two in Switzerland

The Model Rules provide for the implementation of the IIR with effect from January 1, 2023, and the UTPR with effect from January 1, 2024.[40] While most EU Member States initially indicated that they aimed to implement the minimum taxation rules in accordance with the OECD timeline, i.e., starting January 1, 2023, a more realistic timeline for implementation would now seem to be some time during 2024.

Switzerland has also been consistently working towards the implementation of the Model Rules in its domestic jurisdiction. However, the Swiss legislative process is slow in comparison to that of other jurisdictions. The implementation of Pillar Two is complicated by the fact that it entails an amendment to the Swiss federal constitution with regard to the competences of the federation and tax harmonization between the Swiss cantons, as well the principles of universality and uniformity of taxation and taxation that respects the taxpayer's ability to pay. There are still numerous uncertainties and outstanding questions regarding the technicalities of the Model Rules, which are not expected to be fully resolved before the end of 2022. Many

---

[35] *Erläuternder Bericht zum Bundesbeschluss über eine besondere Besteuerung grosser Unternehmensgruppen (Umsetzung des OECD/G20-Projekts zur Besteuerung der digitalen Wirtschaft), dated March 11, 2022, ("Erläuternder Bericht"), p.26/59, last visited May 25, 2022; Daniel Gentsch/Alain Horat, loc. cit., p. 135.*

[36] *Model Rules, art. 8.1.1.*

[37] *Model Rules, art. 8.1.2.*

[38] *Model Rules, art. 8.1.4.*

[39] *Model Rules, art. 8.1.8.*

[40] *Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy, dated October 8, 2022, p.5.*

aspects of the rules are subject to interpretation and will probably only be clarified once a practice has been established.

Against this background, the OECD's published timeline is too ambitious for the Swiss legislative process to accommodate and Pillar Two cannot be expected to be implemented in Swiss domestic law before January 1, 2024.[41] To address timing constraints and uncertainties, Switzerland is planning to implement the Model Rules in two steps.[42] In the first step, Switzerland will amend its Federal Constitution, which will empower the Federal Council to implement Pillar Two based on a federal ordinance. This federal ordinance will then remain valid until the enactment of a formal federal act by the Swiss Federal Parliament. In the second, later step, the provisions of this initial ordinance will be updated and converted into a formal federal act. This two-step approach will allow Switzerland to deal with the time pressure and incorporate already gained experience into the subsequent federal act.

The Swiss Federal Council initiated the legislative consultation procedure on March 11, 2022.[43] Professional organizations and the cantons have submitted a number of statements that broadly agree with the suggested two-step approach. The Federal Council adopted its dispatch on the constitutional amendment on June 23, 2022 for the attention of the Federal Parliament. This will be debated in the fall and winter sessions 2022.[44] The issuance of the first draft of the federal ordinance is scheduled for August 2022. The mandatory referendum for the amendment of the Federal Constitution is scheduled for June 18, 2023. Provided the amendment of the constitution passes the referendum, both the constitutional amendment and the Swiss Federal Council's temporary ordinance on the implementation of Pillar Two should enter into force on January 1, 2024. There are currently no plans to introduce Pillar Two measures in Switzerland with retroactive effect in view of the rule of law that prevents measures being introduced retroactively.[45]

From a Swiss tax perspective, Swiss-headquartered MNE Groups are not expected to face any changes as a result of the GloBE rules prior to 2024, because implementation of the rules in Switzerland will not occur before that date and the UTPR will not apply before 2024 according to the timeline published by the OECD. However, if other jurisdictions implement the IIR as soon as January 1, 2023, foreign MNE Groups with Constituent Entities in Switzerland may already be subject to Pillar Two taxation in other countries in 2023. If the jurisdiction in which a parent company is domiciled has already introduced the IIR in 2023, this jurisdiction may impose taxes on the GloBE Income of Swiss Constituent Entities that are not yet taxed at the 15% global minimum tax rate (the Top-Down approach).

In the short term, the top-up tax is expected to result in additional tax revenues in the range of some 1-2.5 billion Swiss francs in Switzerland.[46] The plan is to allocate 25% of the revenues derived from

---

[41] *Erläuternder Bericht, p.19/59.*

[42] *Erläuternder Bericht, p. 18-19/59.*

[43] *Press Release of March 3, 2022, https://www.sif.admin.ch/sif/de/home/dokumentation/medienmitteilungen/medienmitteilungen.msg-id-87569.html, last viewed May 27, 2022.*

[44] *Press release from the Swiss Federal Council dated June 23, 2022, https://www.admin.ch/gov/en/start/documentation/media-releases.msg-id-89425.html, last visited July 15, 2022.*

[45] *Erläuternder Bericht, p. 18-19/59.*

[46] *Erläuternder Bericht, p. 36.*

Switzerland's domestic top-up tax to the Federation, which must be used budget-neutrally for inter-cantonal fiscal equalization measures and to promote Switzerland's appeal as a business location. The other 75% will go to the cantons imposing the top-up tax and their municipalities. While the cantons have autonomous power to decide on how to use their shares in the revenues from the top-up tax, the intention is again to use these funds to safeguard their appeal as business locations.

In the long term, however, there are fears that Switzerland may lose its tax attractiveness for MNE Groups. Discussions are therefore underway as to how Switzerland's tax attractiveness may be further enhanced (for example, by introducing a tonnage tax or by reducing fiscal burdens that are not Covered Taxes), as well as to how Switzerland's general competitive appeal may be promoted by other means (for example, by increasing funding for R&D and other innovative activities).